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Nos. 85-1658, 85-1660

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

FEDERAL COMMUNICATIONS COMMISSION and
UNITED STATES OF AMERICA,
Appellants,

v.

FLORIDA POWER CORPORATION, *et al.*,
Appellees.

GROUP W CABLE, INC., *et al.*,
Appellants,

v.

FLORIDA POWER CORPORATION, *et al.*,
Appellees.

On Appeals from the United States Court of Appeals for the Eleventh Circuit

BRIEF OF ASSOCIATION OF AMERICAN RAILROADS AS *AMICUS CURIAE*

J. THOMAS TIDD
KENNETH P. KOLSON

ASSOCIATION OF AMERICAN RAILROADS
50 F Street, N.W.
Washington, D.C. 20006
(202) 639-2100

PAUL A. CUNNINGHAM*
RICHARD B. HERZOG
RUSSELL M. BLAU
PEPPER, HAMILTON & SCHEETZ

1777 F Street, N.W.
Washington, D.C. 20006
(202) 842-8191

Attorneys for the Association of American Railroads

* *Counsel of Record*

PRESS OF BYRON S. ADAMS, WASHINGTON, D.C. (202) 347-8203

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INTEREST OF THE *AMICUS CURIAE*

This case is an appeal from a decision of the United States Court of Appeals for the Eleventh Circuit

(hereinafter, the "Eleventh Circuit") holding unconstitutional the provisions of the Pole Attachments Act, 47 U.S.C. § 224, prescribing the maximum amount of compensation payable to a public utility for the physical attachment of television cables to its poles. Although the Pole Attachments Act by its terms does not apply to railroads, 47 U.S.C. § 224(a)(1), railroad property can be used for non-rail-transportation purposes, which uses may raise issues analogous to those in this case.

The Association of American Railroads ("AAR"), an unincorporated association headquartered in the District of Columbia, is the largest organization of railroads in the United States.[1] AAR members carry over 95 percent of the Nation's railroad freight. Class I (major) railroads control more than 150,000 linear miles of right-of-way, on which their tracks are laid. *Railroad Facts 1985 Edition* 42. These rights-of-way span the continent, connecting cities and towns in all of the 48 contiguous States.

AAR has a direct interest both in the authority of government to regulate non-rail uses of railroad rights-of-way, and in the manner in which that authority may be exercised. The position of railroads as owners of rights-of-way is in many ways like that of Appellee Florida Power as an owner of utility poles. The primary use of the rights-of-way, for operating railroads, is subject to government regulation, as is Florida Power's use of its poles in connection with

[1] AAR files this brief by the consent of the parties, pursuant to Rule 36.2 of the Rules of this Court. The parties' letters of consent have been filed with the Clerk.

transmitting electricity.[2] And, just as Florida Power's poles are useful for secondary, non-utility purposes such as attachment of television cables, so rail rights-of-way may be useful for secondary, non-rail purposes such as installation of communications facilities, pipelines, or other items. For example, the Federal Communications Commission ("FCC") has in several cases authorized the construction of fiber-optic communications systems (which can carry high-speed data transmissions and voice communications) in railroad rights-of-way.[3] It is often more efficient for new uses to share existing rights-of-way than to require the construction of all-new pathways; society thereby benefits by deriving additional value from the more productive use of existing assets. Regulation may have a substantial effect on society's ability to obtain these economic benefits, particularly with respect to the efficient deployment of new communications technologies.

AAR supports the affirmance of the Eleventh Circuit's decision; however, we shall not repeat in this

[2] There are substantial differences between the regulation of railroads and of electric utilities. Most significantly, railroad rates are subject to regulatory limitation only in limited circumstances. *See* 49 U.S.C. § 10701a. Railroads, unlike most public utilities, are subject to competition in nearly all of the markets they serve. *See* Staggers Rail Act of 1980, Pub. L. 96-448, § 2(3), 94 Stat. 1895, 1896 (1980). Nonetheless, railroads, like public utilities, are subject to comprehensive regulatory schemes.

[3] *See, e.g., Lightnet*, 58 R.R.2d (P&F) 182, 183 (1985). Indeed, fiber-optic systems can also be attached to utility poles, ducts, and rights-of-way. *See Institutional Communications Co.*, 54 R.R.2d (P&F) 1178, 1179 n.1 (1983). The Pole Attachments Act, however, does not apply to attachments for any purpose other than cable television. 47 U.S.C. § 224(a)(4).

brief the arguments presented by Florida Power and the other Appellees in their briefs on the merits. Rather, AAR submits this *amicus* brief to respond to suggestions made by the Solicitor General and the FCC that could tend to expand the issues in this case beyond those necessary to its decision.

SUMMARY OF ARGUMENT

The narrow constitutional issue in this case is whether Congress, having chosen to require that pole attachments be permitted on "just and reasonable" terms and conditions, may prescribe a binding rule for determining the compensation to be paid for that compelled use of private property. Whether the Court finds the challenged aspect of the Pole Attachments Act valid or not, it need not address in this case the merits of government regulation of non-utility uses of utility property, or the standards for efficient or equitable allocation as between shareholders and ratepayers of the return on the economic value of those uses.

Utility assets can sometimes be used to produce ancillary non-utility services at less cost than those services would require if produced with separate assets. Regulators must determine whether and to what extent the additional value derived from the non-utility use of the asset should benefit ratepayers (by reducing the cost of utility service) or shareholders (by increasing their overall return on investment). Although the Pole Attachments Act requires the attribution of some pole costs to cable television users, the Government's characterization of the Act as a "typical" regulatory scheme is inaccurate. The Government contends that there can be no facial constitutional infirmity in the Act without calling into question standard regulatory practice; to hold the Act unconstitutional, so the argument goes, would bar the regulatory treatment of choice.

By arguing that the Act incorporates a traditional regulatory choice, the Government invites the Court to base its decision on an unnecessary assumption as to the acceptability or wisdom of such attribution of costs in general. Because this case involves only Congress' prescription of an upper limit of compensation, and not the merits of the underlying decision to regulate pole attachments, we urge the Court to avoid sanctioning the Act as a typical or desirable scheme of regulation.

ARGUMENT

I. The Government's Argument Concerning Allocation Of Pole Costs Implicates Issues That Are Not Properly Before The Court

In the Pole Attachments Act, Congress chose to regulate the use of utility property (poles) for non-utility purposes. At the time the Act was adopted, the rates charged by utilities for pole attachments generally were not regulated by the States, unlike their rates for electric or telephone services. S. Rep. No. 580, 95th Cong., 1st Sess. 17 (1977). Nearly all States had determined that pole attachments were not utility services, and were not within the jurisdiction of regulatory agencies under State law.[4]

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[4] *See, e.g., Ceracche Television Corp. v. New York Pub. Serv. Comm'n,* 49 Misc. 2d 554, 267 N.Y.S.2d 969, 973 (N.Y. Sup. Ct. 1960); *International Cable T.V. Corp. v. All Metal Fabricators, Inc.,* 66 P.U.R.3d 446, 463 (Cal. P.U.C. 1966); *WCOG,*

Congress overrode the decision of those States to treat pole attachments as unregulated services, and dictated an allocation of pole costs between ratepayers and cable television companies. The issue before the Court is whether the prescription of a statutory limitation on compensation is constitutionally permissible. The issue is not the more general regulatory policy issue of how ancillary uses of utility assets should be treated in the absence of such a statutory prescription.

The use of utility assets for multiple purposes raises issues of the proper allocation of costs and benefits. Under well-established principles of public utility law, the total amount a utility may charge its ratepayers is limited to the cost of providing its utility service, including the cost of the capital used in producing the service (the "return on investment").[5] Where the same assets are used to produce multiple utility services (*e.g.*, local and long-distance telephone service), the regulatory authority may choose to allocate costs among the various services in order to prescribe reasonable rates for each (although it may also consider other variables). Similarly, where the utility assets are used in part to produce an unregulated service, the regulator seeks to set rates for utility customers that

Inc. v. Southern Bell Tel. & Tel. Co., 64 P.U.R.3d 314, 317 (N.C. Util. Comm'n 1966). The adoption of the Pole Attachments Act did not necessarily alter State law limiting the definition of "utility" services. *Illinois-Indiana Cable Assoc., Inc. v. Indiana Pub. Serv. Comm'n*, 427 N.E.2d 1100, 1110-12 (Ind. Ct. App. 1981). Therefore, the FCC's determination of pole attachment rates does not necessarily affect the State's regulation of utility rates.

[5] *See FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944).

do not cross-subsidize, and are not improperly increased by, costs properly attributable to other services. *See Oklahoma Natural Gas Co.*, 52 P.U.R.3d 180, 181-82 (Okla. Corp. Comm'n 1963), *aff'd sub nom. Oklahoma ex rel. Nesbitt v. Oklahoma Natural Gas Co.*, 406 P.2d 273 (Okla. 1965).

Rational cost attribution presents little problem where, as a matter of fact, the non-utility uses impose new costs, whether fixed or variable. For example, the new use may impose costs for attachment devices, protective equipment for the existing system, and legal costs in perfecting easements originally granted for the utility purposes. Economic theory teaches that efficiency is served by attributing costs to those who cause them. Regulatory agencies do not require utility ratepayers to pay costs that are caused by non-utility activities.

Often, however, the costs of utility assets are not significantly increased by non-utility uses. The cost of right-of-way, or of an electric or telephone pole, may be largely unaffected by the attachment of coaxial or other cable; indeed, most pole costs are the same regardless of whether the pole is used for electric, telephone, or television service, or for any combination of these in any proportion. These are "joint" or "common" costs, and efficiencies result from use of the joint and common costs to produce multiple services ("economies of scope"). *See* 1 A. Kahn, *Economics of Regulation* 77-79 (1970). No single use of the pole "causes" the joint or common costs in the "but for" sense of causation.

When economies of scope exist, the regulator must decide whether the value of the non-utility use of a regulated asset should benefit the utility's sharehold-

ers or its ratepayers. Absent the ancillary use, of course, the entire cost of the pole or other asset would be included in the utility's revenue requirement. If some portion of the joint or common cost is attributed to a non-utility service, then the regulator may justify reducing utility rates; to that extent, ratepayers benefit from the non-utility use. In that case, the total earnings of the utility do not necessarily increase by reason of the ancillary use, but the revenue requirement is divided between ratepayers and non-utility users of the asset. By contrast, if joint and common costs remain in the utility's cost of service, its shareholders will benefit from the return (if any) generated by the non-utility use, just as they would in any unregulated enterprise.

The Pole Attachments Act allocates benefits to utility ratepayers by assigning a portion of pole costs to cable television users, even though those costs would have had to be paid even in the absence of the cable attachment. The United States and the FCC seem to suggest in their brief on the merits ("Govt. Br.") that the choice is typical—that regulators ordinarily reallocate the benefits of ancillary uses of utility assets:

> The utility's total annual revenue is typically fixed by the state agency to reflect its perceived overall revenue requirements. *Funds derived from pole attachment fees help defray costs that would otherwise be borne by the utility's customers.* The determination of the proper allocation of costs between different kinds of utility customers is the essence of the business of utility regulatory agencies. In this context, *the cable companies are in effect simply another kind of customer,* and state

> regulation of the rates charged them by the utilities would be no less consistent with the Just Compensation Clause than is any other component of the state rate regulation scheme.

Govt. Br. 11 (emphasis supplied). This passage suggests that the decision below implicates all rate setting by regulatory agencies. Allocation of costs among customers is a typical regulatory function, so the argument goes; the efficient or fair approach is to treat the cable operator as simply another customer; and the Act performs a typical regulatory function in deciding how certain costs are to be attributed to that customer.[6] Accordingly, the Government contends, there can be no facial constitutional infirmity in the Act without calling into question standard regulatory practice; to hold the Act unconstitutional would bar the regulatory treatment of choice; and any proper constitutional challenge involving the Act could concern only whether a particular rate was confiscatory.

The Government's portrayal of supposedly typical regulation, in combination with the impact of decisions by the Court on rate regulatory issues generally, seems to invite the Court to speak in terms that

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[6] In similar vein, the federal appellants reject as "overdrawn and wholly immaterial for purposes of allocating pole costs among the users" Florida Power's argument that in leasing space on its poles "it is acting not 'in its role as a public utility rendering electric service to the public, but rather in its non-utility role as a renter of space on its property * * *.' " Govt. Br. 11, n.12. We would note, however, that in many cases regulators have found this distinction to be highly material for purposes of allocating costs. *See Oklahoma Natural Gas Co., supra,* and cases cited *supra* note 4.

appear to sanction regulatory transfers of the returns from non-utility uses as a matter of theory and practice. Any such doctrinal consequences would be premature and unwise. The Court can, of course, agree or disagree that the Act encroaches upon Article III powers without deciding whether the regulation of ancillary uses of utility property is preferable or required as a matter of general regulatory theory.[7] AAR's purpose in this brief is to suggest that, however the Court resolves the constitutional issue, it make unmistakably clear that it is not resolving or even addressing the allocation issue.

In most constitutional cases, there would be no need for such concern. It is well understood that when the Court passes on the constitutionality of a statute, it is making no judgment as to the wisdom of the statutory policy. Constitutional holdings in rate cases are different, however. The Court's pronouncements on constitutional aspects of ratemaking have often dominated ratemaking law and theory at both the federal and state level. Such cases as *Smyth v. Ames*,[8] Justice Brandeis' concurrence in *Southwestern Bell Telephone*,[9] *Bluefield Water Works*,[10] and *Hope Natural Gas*,[11] attained significance not only as statements of

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[7] The Court could also decide whether the rate that results under the statutory formula is confiscatory without deciding whether such formulaic allocation is proper or preferable as a matter of general rate theory.

[8] 169 U.S. 466 (1898).

[9] *Missouri ex rel. Southwestern Bell Telephone Co. v. Public Service Commission*, 262 U.S. 276, 290 (1923).

[10] *Bluefield Water Works & Improvement Co. v. Public Serv. Comm'n*, 262 U.S. 679 (1923).

[11] *Supra* note 5.

constitutional boundaries but as paradigms of regulatory theory and policy. It would be most unfortunate if, en route to its decision concerning the constitutionality of this Act, the Court said anything about allocation that attained comparable significance.

The Government's suggestion that the Pole Attachments Act represents a "typical" (and, by further implication, efficient and fair) regulatory scheme papers over a far more complex reality. In the following section, we will show that there is no standard practice or generally applied theory regarding allocation of the benefits of non-utility uses, and discuss some of the more important factors that may affect a particular regulatory decision. In doing so, we do not suggest or seek a resolution of the issues, but intend to illustrate that their unsettled nature belies the Government's assertion that the Act reflects a settled or indisputably preferable regulatory practice.

II. The Allocation Of Utility Costs Requires Consideration Of Numerous Factors That Are Not Contained In The Record, Have Not Been Briefed, And Often Reflect A Particular Regulatory Context

The allocation of joint and common costs is more than a matter of accounting technicalities—it raises issues central to the relationship between a utility and its customers and to the public interest in that relationship. A fundamental underlying issue is whether stockholders who invest in utility assets retain essential ownership rights in their property, including the right to exploit new, valuable uses of that property.

Relieving ratepayers of the need to pay for joint and common costs transfers to them part of the value of the utility's assets, as if they were the owners of the assets. This Court has stated, however, that the

utility-ratepayer relationship does not vest ratepayers with any interest in the assets used to produce the utility service. In *Board of Public Utility Commissioners v. New York Telephone Co.*, 271 U.S. 23 (1926), the Court said:

> Customers pay for service, not for the property used to render it. Their payments are not contributions to depreciation or other operating expenses or to capital of the company. *By paying bills for service they do not acquire any interest, legal or equitable, in the property used for their convenience* or in the funds of the company. Property paid for out of moneys received for service belongs to the company just as does that purchased out of proceeds of its bonds and stock.

271 U.S. at 32 (emphasis supplied). Correspondingly, the government limits the return that investors may earn on utility uses of their assets, but does not deprive them of the right to exploit other uses. As Justice Brandeis remardmark currence in the *Southwestern Bell* case,

> [t]he several items of property constituting the utility, taken singly, and freed from the public use, may conceivably have an aggregate value greater than if the items are used in combination. The owner is at liberty, in the absence of controlling statutory provision, to withdraw his property from the public service; and, if he does so, may obtain for it exchange value.

262 U.S. at 290. Although Justice Brandeis referred to the sale of assets, the same conclusion applies when

the owner can exploit the non-utility value of an asset without withdrawing it from utility service.[12] The key distinction is between the owner's ability to recover appreciation in the value of the utility property *from ratepayers*, and the ability to recover that appreciation from purchasers of other uses of the property.

The *New York Telephone* conceptualization of the ratepayer-utility relationship tends to support allocation to shareholders of the economic value of non-utility uses. It has been so applied, for example, by the Federal Energy Regulatory Commission ("FERC") with respect to sales of appreciated utility property. Where such sales are at prices that exceed the depreciated original cost of the utility asset, FERC allocates the gain to shareholders. *See Virginia Electric & Power Co.*, 27 FERC (CCH) ¶ 61,093, *reh'g denied*, 27 FERC (CCH) ¶ 61,406 (1984); *Duke Power Co.*, 48 F.P.C. 1384, 1394-95 (1972); Order No. 473, 49 F.P.C. 390, 391 (1973).[13]

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[12] Indeed, a lease of an asset may be viewed as economically equivalent to a sale. The sale price in this case is the discounted present value of the rental income stream. The timing or legal form in which economic value is realized should not affect the allocation as between shareholders and ratepayers.

[13] The *New York Telephone* conceptualization has also had a broad effect on regulatory practices in many contexts other than the use of utility assets for non-utility purposes. *See, e.g., Secretary of Defense v. Chesapeake & Potomac Tel. Co.*, 217 Va. 149, 225 S.E.2d 414 (1976) (rejecting contention that rates must be based solely on cost of service); *General Motors Corp. v. Public Serv. Comm'n*, 95 A.D.2d 876, 463 N.Y.S.2d 886, 888 (1983) (rejecting contention that electric utility customers are entitled to "the benefits of the lower running costs of the plants for which their rates have paid").

Other jurisdictions have allowed shareholders to retain the benefits of non-utility uses based on an analysis of cost causation. They have concluded that costs that would be incurred in the absence of a non-utility use should continue to be included in the regulated cost of service, even though those costs may also benefit the non-utility use. *See, e.g., City of El Dorado v. Arkansas Public Service Commission*, 235 Ark. 812, 362 S.W.2d 680, 685 (1962) (rejecting argument that ratepayers of a local gas utility should be relieved of transportation costs that "would accrue whether the gas is processed [the unregulated activity] or piped directly to utility customers").

Various other issues may affect allocation decisions. For example, if benefits from non-utility uses were allocated to ratepayers, utility managements might be indifferent to non-utility uses, in which event ratepayers would continue to bear the costs of excess capacity or otherwise fail to benefit from non-utility uses. *See, e.g., Casco Bay Lines v. Public Utilities Commission*, 390 A.2d 483, 489-90 (Me. 1978) (allowing 90 percent to ratepayers of gain from sale of appreciated utility assets but reserving ten percent to shareholders to create appropriate managerial incentives). Furthermore, if the economic value of non-utility uses were permitted to influence utility rates, regulatory agencies might be drawn into unwanted or unauthorized regulation of otherwise unregulated markets. *See Oklahoma Natural Gas Co., supra*, 52 P.U.R.3d at 182.[14]

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[14] Regulatory agencies do regularly examine utility dealings with affiliated entities that either supply or purchase from the utility, but dealings with affiliates are a special case.

Even in those cases where regulators have chosen to allocate some portion of joint and common costs to non-utility services, they have used many different methods of allocation. In the absence of cost causation, agencies may resort to accounting conventions based on various notions of efficiency or fairness.[15] Costs may be allocated among services based upon some measurement or estimate of usage. *See MCI Telecommunications Corp. v. FCC*, 675 F.2d 408, 410-11 (D.C. Cir. 1982). The upper limit in the Pole Attachments Act is one variant of this accounting approach to "fully allocated" cost. It is generally recognized, however, that no accounting allocation can achieve "purely economic" results. *Id.* at 415-16. An alternative approach holds that economic efficiency, or the allocation of resources to their most-valued uses, is maximized by letting those who value the service the most pay the most. Under this approach, joint and common costs are generally allocated in inverse relation to the elasticity of demand; they are allocated to the most demand-inelastic users of the assets. *See, e.g., Coal Rate Guidelines—Nationwide*, 1 I.C.C.2d 520 (1985). Such value-of-service allocation techniques have long been used, albeit less quanti-

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[15] Regulators have developed two ways of transferring to ratepayers the benefits of non-utility uses. The first method leaves the assets entirely in the utility rate base, but credits revenues received from non-utility uses to the revenue requirements of the utility. To the extent that revenues are so credited, ratepayers are relieved of the necessity to meet the utility's entire revenue requirement. The second method of allocation removes some portion of the assets from the rate base. The revenue requirement borne by ratepayers is reduced by the portion of operating expenses and the cost of capital attributable to the assets so removed.

tatively, in setting telephone rates. *See Secretary of Defense v. Chesapeake & Potomac Telephone Co., supra* note 13.

Some courts have approached allocation matters on a more *ad hoc* basis. In cases where the court believed that the ratepayers bore the risk of loss on particular investments, ratepayers have been held entitled to the benefits of any profit produced by that investment. *See, e.g., Democratic Central Committee v. Washington Metropolitan Area Transit Commission*, 485 F.2d 786, 806 (D.C. Cir. 1973); *cert. denied sub nom. D.C. Transit System, Inc. v. Democratic Central Committee*, 415 U.S. 935 (1974); *New York Water Service Corp. v. New York Public Service Commission*, 12 A.D.2d 122, 208 N.Y.S.2d 857, 863-64, 37 P.U.R.3d 442, 447-48 (1960), *appeal denied*, 13 A.D.2d 610, 214 N.Y.S.2d 667 (1961). Some jurisdictions consider whether depreciation expense was included in the utility's cost of service, and allocate some or all gains upon sale of depreciated assets to ratepayers. *See, e.g., Boise Water Corp. v. Idaho Public Utilities Commission*, 99 Idaho 158, 578 P.2d 1089, 1092-93 (1978) (gain on sale of nondepreciable land allocated to shareholders); *Wyoming Gas Co.*, 40 P.U.R.3d 509, 513 (Wyo. Pub. Serv. Comm'n 1961) (gain on sale of depletable gas reserves allocated to ratepayers).

CONCLUSION

The question of what constitutes an efficient or equitable allocation of the economic value of non-utility uses of utility assets is not before the Court. The question has not been briefed by the parties; AAR's summary in this brief is intended to illustrate the scope of the subject and some of the disparities and

complexities, but does not seek a resolution. Nor is resolution of the question necessary to a decision on the question that is before the Court—whether Congress may statutorily impose an upper limit of compensation for a taking. AAR respectfully asks that the Court avoid any opinion on the merits of the allocation question as a matter of general regulatory theory.

Respectfully submitted,

J. THOMAS TIDD
KENNETH P. KOLSON

ASSOCIATION OF AMERICAN RAILROADS
50 F Street, N.W.
Washington, D.C. 20006
(202) 639-2100

PAUL A. CUNNINGHAM*
RICHARD B. HERZOG
RUSSELL M. BLAU
PEPPER, HAMILTON & SCHEETZ

1777 F Street, N.W.
Washington, D.C. 20006
(202) 842-8191

Attorneys for the Association of American Railroads

**Counsel of Record*

August 29, 1986